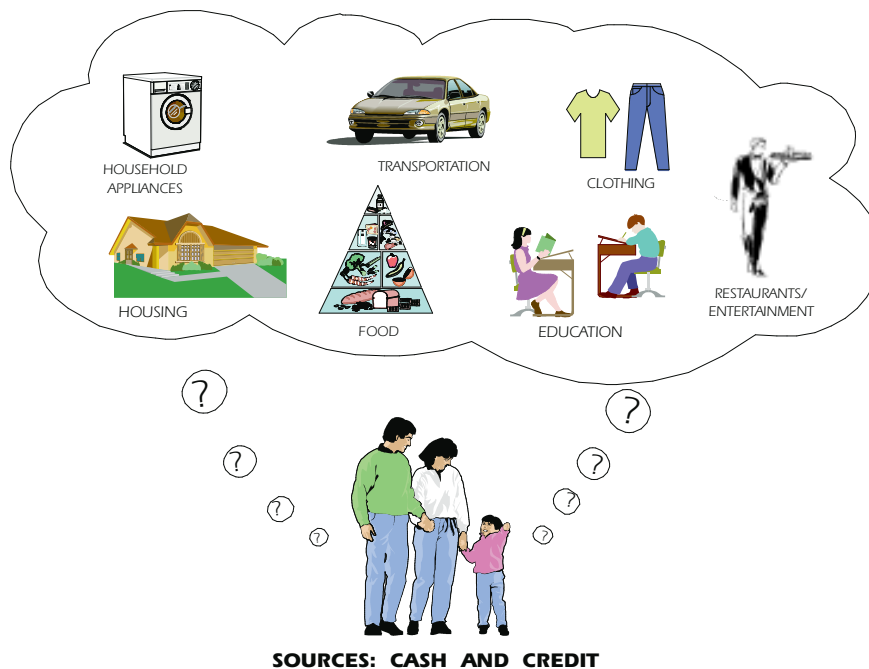


2. Where the Money Comes From— and Where it Goes

In a typical American household, a father and mother might sit around the kitchen table to review the family budget. They might discuss how much they expect to earn each year, how much they can spend on food, shelter, clothing, transportation, and perhaps a vacation, and how much they might be able to save for their future needs.

If they do not have enough money to make ends meet, they might discuss how they can spend less, such as by cutting back on restaurants, movies, or other entertainment. They also might consider whether to try to earn more by working more hours or taking another job. If they expect their shortfall to be temporary, they might try to borrow.

Chart 2-1. Family Budgeting

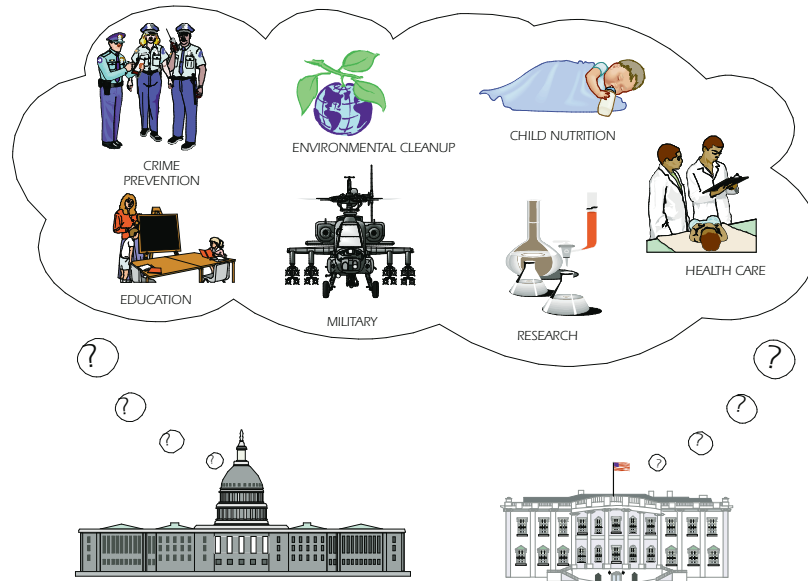


Generally speaking, the Federal Government plans its budget much like families do. The President and Congress determine how much money they expect the Government to receive in each of the next several years, where it will come from, and how much to spend to reach their goals—goals for national defense, foreign affairs, social insurance for the elderly, health insurance for the elderly and poor, law enforcement, education, transportation, science and technology, and others.

They decide how much spending they will finance through taxes and how much through borrowing. They debate how to use the budget to help the economy grow, or to redistribute income. And, especially lately, they debate how to use the budget surplus to address longer-term concerns and invest in the Nation's future.

In this chapter, we will discuss these decisions in some detail—that is, how the Government raises revenues and where it spends money.

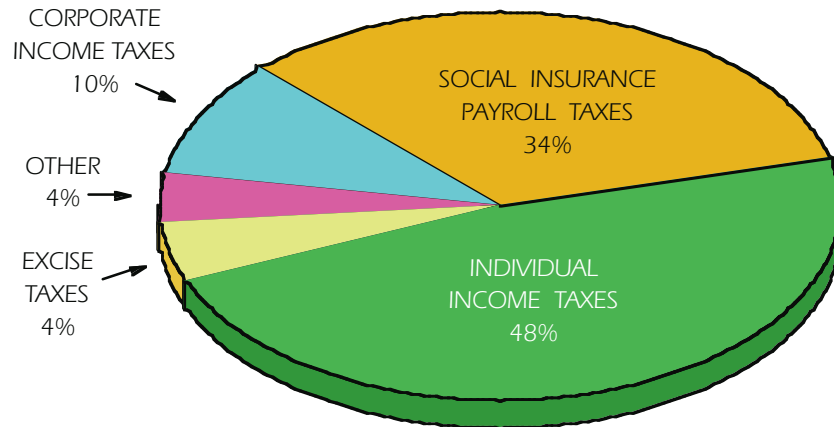
Chart 2-2. National Budgeting



SOURCES: TAXES AND BORROWING

Revenues

**Chart 2-3. The Federal Government Dollar—
Where It Comes From**



The money that the Federal Government uses to pay its bills—its revenues—comes mostly from taxes. In 1998, revenues were greater than spending, and the Government was able to reduce the national debt with the difference between revenues and spending—that is, the surplus.

Revenues come from these sources:

- Individual income taxes will raise an estimated \$900 billion in 2000, equal to about 10 percent of GDP.
- Social insurance payroll taxes—the fastest growing category of Federal revenues—include Social Security taxes, Medicare taxes, unemployment insurance taxes, and Federal employee retirement payments. This category has grown from two percent of GDP in 1955 to an estimated seven percent in 2000.
- Corporate income taxes, which will raise an estimated \$189 billion, have shrunk steadily as a percent of GDP, from 4.5 percent in 1955 to an estimated 2.1 percent in 2000.

Table 2-1. Revenues By Source—Summary

(In billions of dollars)

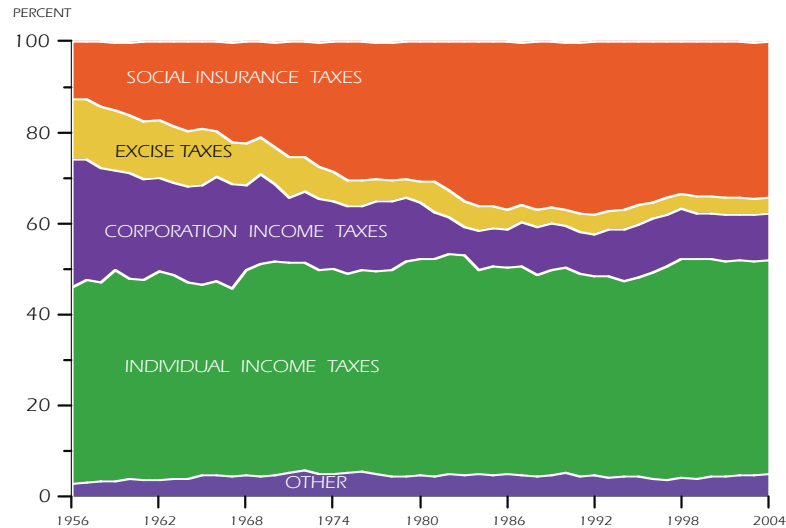
Source	1998 Actual	Estimate					
		1999	2000	2001	2002	2003	2004
Individual income taxes	829	869	900	912	943	971	1,018
Corporate income taxes	189	182	189	197	203	212	221
Payroll taxes	572	609	637	660	686	712	739
Excise taxes	58	68	70	71	72	74	75
Estate and gift taxes	24	26	27	28	30	32	34
Customs duties	18	18	18	20	21	23	25
Miscellaneous receipts	33	35	42	45	50	52	53
Total receipts	1,722	1,806	1,883	1,933	2,007	2,075	2,166

Notes: The revenues listed in this table do not include revenues from the Government's business-like activities—i.e., the sale of electricity and fees at national parks. The Government counts these revenues on the spending side of the budget, deducting them from other spending to calculate its outlays for the year.

Numbers may not add to the totals because of rounding.

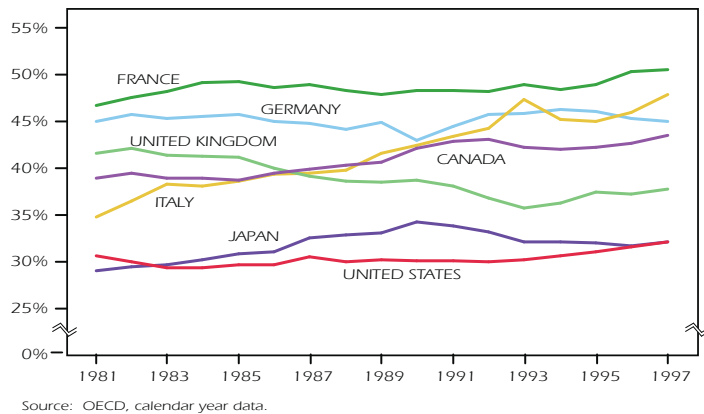
- Excise taxes apply to various products, including alcohol, tobacco, transportation fuels, and telephone services. The Government earmarks some of these taxes to support certain activities—including highways and airports and airways—and deposits others in the general fund.
- The Government also collects miscellaneous revenues—e.g., customs duties, Federal Reserve earnings, fines, penalties, and forfeitures.

Chart 2-4. Composition of Revenues



Between 1960 and 1998, payroll taxes have increased substantially as a percent of total revenues, and corporate income taxes have declined, but individual income taxes have remained roughly constant.

Chart 2-5. Revenues as a Percent of GDP—Comparison With Other Countries



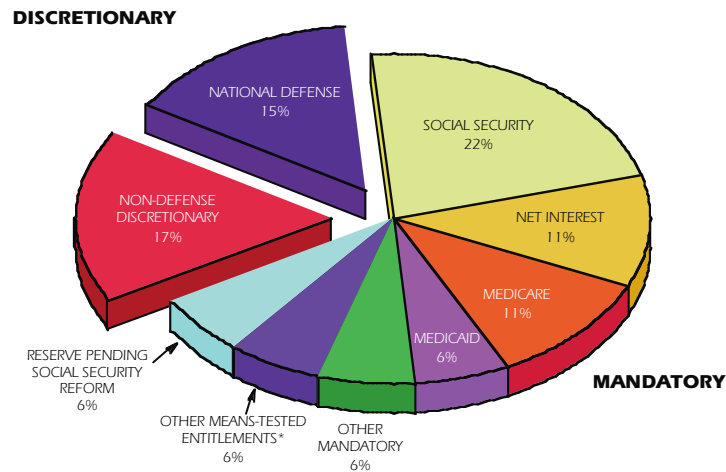
The United States and Japan have the lowest revenues as a percent of GDP of the seven countries shown above.

Spending

As we have said, the Federal Government will spend nearly \$1.8 trillion¹, and have a surplus of over \$117 billion in 2000, which we divided into nine large categories as shown in Chart 2-6.

- The largest Federal program is Social Security, which will provide monthly benefits to nearly 45 million retired and disabled workers, their dependents, and survivors. It accounts for 22 percent of your Federal dollar (or 23 percent of all Federal spending).
- Medicare, which will provide health care coverage for over almost 40 million elderly Americans and people with disabilities, consists of Part A (hospital insurance) and Part B (insurance for physician costs and other services). Since its birth in 1965, Medicare has accounted for an ever-

**Chart 2-6. The Federal Government Dollar—
Where It Goes**



* Means-tested entitlements are those for which eligibility is based on income. The Medicaid program is also a means-tested entitlement.

¹ In calculating Federal spending, the Government deducts collections (revenues) generated by the Government's business-like activities, such as fees to national parks. These collections will total an estimated \$216 billion in 2000. Without them, spending would total an estimated \$2.0 trillion in 2000, not \$1.8 trillion.

growing share of spending. In 2000 it will comprise 11 percent of your Federal dollar (or 12 percent of all Federal spending).

- Medicaid, in 2000, will provide health care services to almost 34 million Americans, including the poor, people with disabilities, and senior citizens in nursing homes. Unlike Medicare, the Federal Government shares the costs of Medicaid with the States, paying between 50 and 83 percent of the total (depending on each State's requirements). Federal and State costs are growing rapidly. Medicaid accounts for six percent of your Federal dollar (also six percent of the budget).
- Other means-tested entitlements provide benefits to people and families with incomes below certain minimum levels that vary from program to program. The major means-tested entitlements are Food Stamps and food aid to Puerto Rico, Supplemental Security Income, Child Nutrition, the Earned Income Tax Credit, and veterans' pensions. This category will account for an estimated six percent of your Federal dollar (also six percent of the budget).
- The remaining mandatory spending, which mainly consists of Federal retirement and insurance programs, unemployment insurance, and payments to farmers, comprises six percent of your Federal dollar (also six percent of the budget).
- National defense discretionary spending will total an estimated \$275 billion in 2000, comprising nearly 15 percent of your Federal dollar (and 16 percent of the budget).
- Non-defense discretionary spending—a wide array of programs that include education, training, science, technology, housing, transportation, and foreign aid—has shrunk as a share of the budget from 23 percent in 1966 to an estimated 18 percent in 2000 (or 17 percent of your Federal dollar).
- Interest payments, primarily the result of previous budget deficits, averaged seven percent of Federal spending in the 1960s and 1970s. But, due to the large budget deficits that began in the 1980s that share quickly doubled to 15 percent. Since the budget is now in surplus, interest payments are estimated to drop to 12 percent of the budget in 2000 (11 percent of your Federal dollar).
- Six percent of your Federal dollar (the budget surplus) will not be spent. The President has proposed that any surplus be reserved until a plan to save Social Security has been enacted.

Table 2-2. Spending Summary

(In billions of dollars)

	1998 Actual	Estimate					
		1999	2000	2001	2002	2003	2004
Budget Policy with Social Security reform:							
Outlays:							
Discretionary:							
Department of Defense	258	265	262	269	279	291	301
Non-DoD discretionary	297	317	330	341	339	338	338
Priority initiatives				2	4	7	10
Subtotal, discretionary	555	581	592	612	623	636	649
Mandatory:							
Programmatic:							
Social Security	376	389	405	424	444	465	487
Medicare and Medicaid	291	311	328	350	363	391	416
Means-tested entitlements (except Medicaid)	99	107	112	118	124	129	134
Deposit insurance	-4	-5	-2	-2	-1	-*	1
Other	92	117	116	118	115	125	131
Subtotal, mandatory	855	919	959	1,007	1,044	1,110	1,170
Net interest	243	227	215	207	197	188	179
Subtotal, mandatory and net interest	1,098	1,146	1,174	1,214	1,241	1,297	1,349
Total, outlays	1,653	1,727	1,766	1,826	1,863	1,934	1,998
Receipts	1,722	1,806	1,883	1,933	2,007	2,075	2,166
Resources contingent upon Social Security reform:							
Department of Defense				-10	-17	-13	-15
Non-DoD discretionary				-15	-20	-16	-9
Priority initiatives				-2	-4	-7	-10
Related debt service				-1	-2	-4	-6
Total				-27	-43	-41	-40
Reserve pending Social Security reform	69	79	117	134	187	182	208
Surplus	0	0	0	0	0	0	0
MEMORANDUM:							
Discretionary totals if no Social Security reform is enacted, net of designated offsets.	555	581	574	573	568	584	600

* \$500 million or less.

Table 2-3. Total Spending by Function

(Outlays, in billions of dollars)

Function	1998 Actual	Estimate					
		1999	2000	2001	2002	2003	2004
National defense:							
Department of Defense-Military	256	264	261	269	278	290	300
Other	12	13	13	14	14	14	14
Total, national defense	268	277	274	282	292	304	314
International affairs	13	15	16	17	18	18	18
General science, space, and technology . . .	18	19	19	19	19	19	19
Energy	1	*	-2	-1	-1	-1	-1
Natural resources and environment	22	24	24	24	24	24	24
Agriculture	12	21	15	13	11	10	10
Commerce and housing credit	1	*	6	8	9	10	10
Transportation	40	43	46	49	50	52	53
Community and regional development	10	10	10	10	10	9	9
Education, training, employment, and social services	55	60	63	68	67	69	70
Health	131	143	152	163	173	185	197
Medicare	193	205	217	231	235	252	266
Income security	233	243	258	267	275	282	291
Social security	379	393	409	427	447	468	491
Veterans benefits and services	42	44	44	45	46	47	48
Administration of justice	23	24	28	29	28	28	28
General government	13	15	14	15	15	15	15
Net interest	243	227	215	206	195	183	173
Allowances		3	3	-27	-40	-34	-29
Undistributed offsetting receipts	-47	-40	-46	-45	-51	-47	-48
Total	1,653	1,727	1,766	1,799	1,820	1,893	1,958

* \$500 million or less.

Note: Spending that is shown as a minus means that receipts exceed outlays.

Numbers may not add to the totals because of rounding.

Table 2-4. Discretionary Spending by Agency

(Outlays, in billions of dollars)

Agency	1998 Actual	Estimate					
		1999	2000	2001	2002	2003	2004
Legislative Branch	2	2	3	3	3	3	3
Judicial Branch.	3	3	4	4	4	4	4
Agriculture.	16	17	16	15	15	15	15
Commerce.	4	5	7	5	5	5	5
Defense-Military	258	265	262	269	279	291	301
Education	26	29	32	35	35	35	35
Energy	17	17	18	18	18	18	18
Health and Human Services	35	39	42	43	43	43	43
Housing and Urban Development.	33	33	34	34	32	31	30
Interior	7	8	8	9	9	9	9
Justice.	15	16	19	20	19	19	19
Labor	10	11	11	11	11	12	12
State	5	6	6	7	7	6	7
Transportation	37	40	43	46	48	49	51
Treasury.	11	12	12	13	13	13	13
Veterans Affairs	18	19	19	19	19	19	19
Corps of Engineers.	4	4	4	4	4	4	4
Other Defense Civil Programs	*	*	*	*	*	*	*
Environmental Protection Agency	7	7	7	8	7	7	7
Executive Office of the President	*	*	*	*	*	*	*
Federal Emergency Management Agency . .	3	3	3	3	2	2	2
General Services Administration.	1	*	*	*	*	*	*
International Assistance Programs	11	12	12	12	13	12	12
National Aeronautics and Space Administration	14	14	13	13	13	14	14
National Science Foundation	3	3	4	4	4	4	4
Office of Personnel Management	*	*	*	*	*	*	*
Small Business Administration	1	1	1	1	1	1	1
Social Security Administration	5	6	6	6	6	6	6
Other Independent Agencies	6	6	6	6	7	7	7
Allowances		3	3	-24	-36	-29	-24
Undistributed offsetting receipts			-3	1	1	—*	—*
Total	555	581	592	586	582	600	615

* \$500 million or less.

Note: Discretionary spending is appropriated by the Congress each year, in contrast with mandatory spending, which is automatic under permanent law. For a more complete discussion of discretionary spending, see "Action in Congress" in Chapter 3.

Spending that is shown as a minus means that receipts exceed outlays.

Numbers may not add to the totals because of rounding.

“On” and “Off” Budget

From time to time, you may hear about programs that are “off-budget,” meaning that the Government categorizes them separately from other programs.

Specifically, the law requires that the spending and revenues of two Federal programs, Social Security and the Postal Service, be excluded from the budget totals—that is, categorized as “off-budget.” Therefore, the budget displays “on-budget,” “off-budget,” and “unified budget” totals to satisfy this legal requirement.

The unified budget is the most useful display of the Government’s finances; it is vital in calculating how much the Government has to borrow.

The “off-budget” category is designed to give special status to certain programs. Over the years, the Government has placed numerous programs “off-budget,” then returned them to the unified budget. But the mere listing of programs as “off-budget” does not, by itself, protect them from the budget process—e.g., Administration and congressional review, possible cuts, and hiring and procurement rules.

Chart 2-7 illustrates the relationship between on- and off-budget items, and the unified budget.

Chart 2-7. On- and Off-Budget Deficit Projections

